



HOME EQUITY LENDING TRENDS **HOME EQUITY LENDING IS ON THE REBOUND** **AND THE UNTAPPED POTENTIAL IS HUGE**

A whitepaper examining the recent uptick in home equity lending and future home equity lending opportunities for financial institutions.

BY STEVE SCHIPPER, CFA
Founder and Managing Director, LendTrade

It has been seven long years since the housing bust of 2008-2009. During this time, home equity lending activity was severely dampened as home values stagnated or plummeted.

But the home equity lending market is starting to stage a comeback. According to Equifax, home equity loan origination volumes have been trending sharply higher the past couple of years. In 2015, lenders originated home equity lines of credit with limits of \$146.1 billion. This was the highest level of HELOC lending since 2008 and double the HELOC volume of 2011 when it plunged to just \$73.2 billion.

It also represented the fourth consecutive year of growth in HELOC volume and was up 20 percent over 2014. In fact, HELOC originations have risen in each of the last 18 quarters, according to CoreLogic.

We've still got a long ways to go before we get back to the pre-crash heyday of HELOC lending — like when originations consistently exceeded \$400 billion a year between 2002 and 2006. “But there are clear signs that a continually improving real estate market, a strengthening economy and better loan performance are converging to increase the lending community’s comfort level with home equity products,” noted a new whitepaper on the Home Equity Lending Landscape recently released by CoreLogic.

REASONS FOR THE REBOUND

According CoreLogic, 1.4 million homeowners are highly likely to take out a home equity loan or line of credit in the next six months. It cites two main reasons for the rebound in home equity lending and this bullish forecast: home price appreciation and job growth, both of which boost consumer confidence. According to the S&P/Case-Shiller Home Price Index, home prices are now up 35 percent since 2012 and the average home price is now within 5 percent of its peak a decade ago.

In particular, strong price appreciation in most U.S. markets has significantly reduced negative equity at the bottom of the market. This has created more than \$6 trillion worth of equity since early 2009. Also, about 30 million homeowners now own their homes free and clear. On the employment front, meanwhile, more than 13.5 million new jobs have been created over the past six years and the unemployment rate has been cut in half.

The CoreLogic whitepaper also revealed that the number of homeowners with loan-to-value ratios (LTVs) of between 50% and 75% is rising steadily. The number of mortgages with this much equity hit 18 million during the second quarter of last year, up from 11 million in the third quarter of 2009.

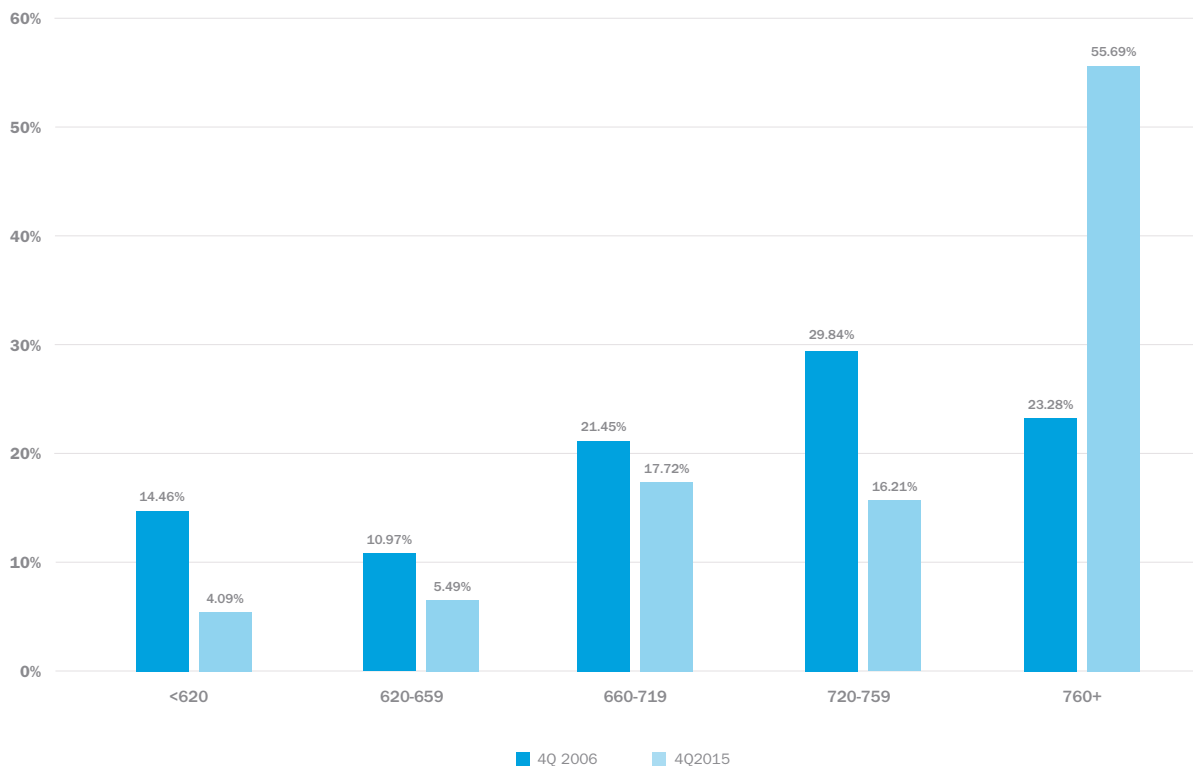
And the number of mortgages with 50% or lower LTVs increased from 11.3 million to 15.4 million during the same period. These borrowers could represent the prime target market for HELOCs in the future when they need to finance major expenditures like their kids' college educations and weddings and large out-of-pocket medical expenses.

“There are clear signs that a continually improving real estate market, a strengthening economy and better loan performance are converging to increase the lending community’s comfort level with home equity products.”

-Home Equity Lending Landscape,
published by CoreLogic



MORTGAGE ORIGINATIONS BY CREDIT SCORE



Source: New York Fed Consumer Credit Panel/Equifax



MORE CONSERVATIVE UNDERWRITING

Not surprisingly, the underwriting for HELOCs being originated today is more conservative than it was before the crash — back in the days of 100% CLTVs, DTIs of 50% or higher, stated income loans and FICO scores in the 600s. For example, consider these “now vs. then” statistics:

Average combined loan-to-values (CLTVs):

2005: 75%

2015: 61%

Average debt-to-income ratios (DTIs):

2005: 38%

2015: 34%

Average FICO score:

2005: 733

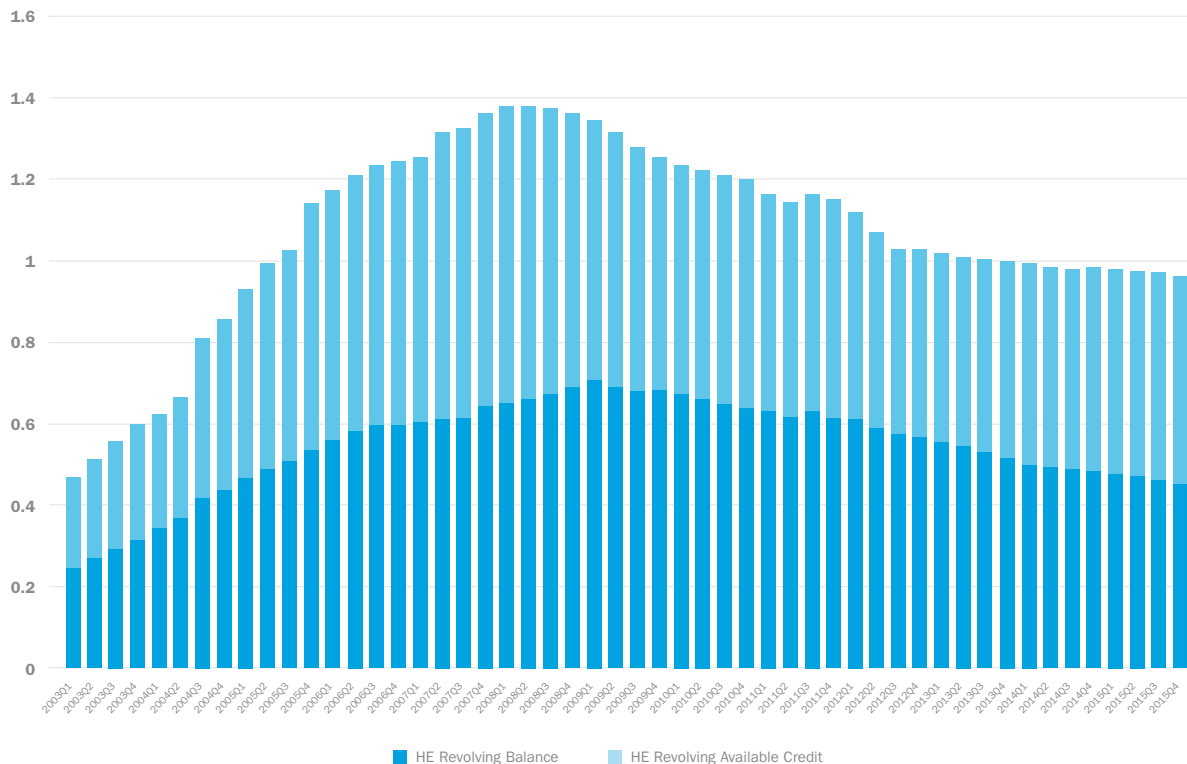
2015: 774

LendTrade has been working with a number of home equity origination firms that can produce more loans and lines than they can hold for the long-term. In general, these firms are selling loans with weighted average CLTVs in the high 80s, weighted average FICO scores in the 750+ range, and DTIs in the low 30s. The majority of these opportunities have been for HELOCs and tend to be piggyback originations.

But we expect that going forward, more of the production will consist of standalone second mortgages as borrowers looking to tap home equity choose to leave their existing first mortgages in place. Additionally, a number of the firms we're working with are using insurance to protect themselves from credit losses for second liens with CLTVs up to 95%.



HELOC AVAILABLE LINES AND OUTSTANDING BALANCES



Source: FRB, Equifax, Consumer Credit Panel
Includes all federally insured banks and credit unions

UNTAPPED HOME EQUITY POTENTIAL

There appears to be a large well of untapped potential for home equity lending in the near future. For example, there were 12.6 million properties in the U.S. at the end of last year that were “equity-rich,” or had at least 50 percent equity. This represented 22.5 percent of all properties with a mortgage and was up by 2.1 million properties over the third quarter of last year and by 1.4 million properties at the end of 2014. Also, while HELOC line amounts are rising, HELOC initial utilization rates are near 10-year lows.

A resurgence in home remodeling is another factor that’s driving the surge in home equity lending and bullish forecasts for the future. At the end of 2015, the National Association of Homebuilders’ Remodeling Market Index remained above the key breakeven mark of 50 for the 10th consecutive quarter. This indicates confidence among remodelers about the market.

With home price appreciation holding steady in the low- to middle-single digit range annually, many homeowners feel more confident investing in their

homes. A recent survey by Bankrate.com found that 28 percent of all homeowners (or 36 million of them) plan to renovate their homes within the next year.

Also, The Home Depot and Lowe’s both recently offered upbeat forecasts for the next few years, and an RBC Capital Markets analyst recently told his clients that they don’t believe investors are starting to sour on the home improvement sector. The Leading Indicator of Remodeling Activity (LIRA) projects that spending on home remodeling projects will increase by 8.6% by the end of this year and by 9.7% by the first quarter of next year. Harvard University’s Joint Center for Housing Studies expects the level of annual spending for remodeling and repairs to reach \$325 billion by early 2017, which will be the highest level in a decade.



Another positive factor for home equity lending is the desire among homeowners with low rates (i.e., under 4%) on their primary 30-year fixed-rate mortgages to not lose these by moving into a new home. More than half of the current tappable home equity resides in mortgages with rates lower than 4% and the average

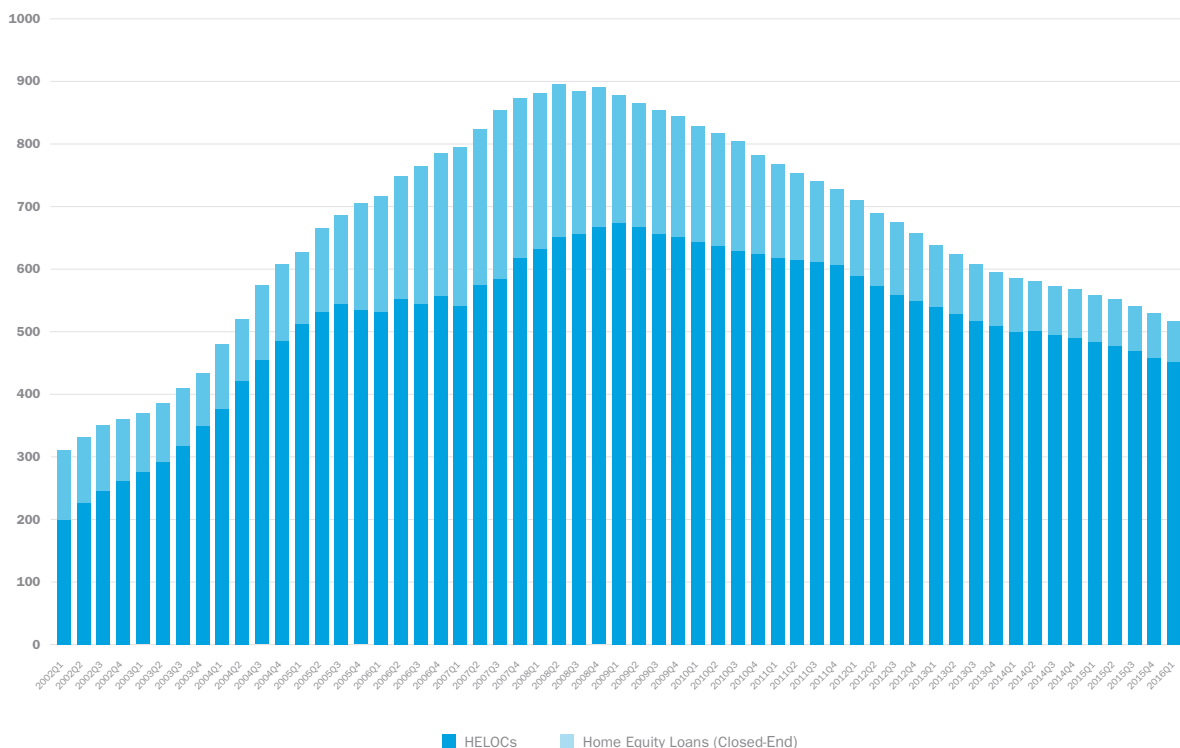


rate on outstanding mortgage debt is now 3.8%. While rates on 30-year fixed-rate mortgages are expected to remain below 4.5% on an annualized basis this year, the Mortgage Bankers Association projects that they will rise to an average of 4.7% next year and 5.2% in 2018.

It's not a given that homeowners won't refinance into a higher rate to tap home equity. But in general, HELOCs are a more attractive way to tap home equity than cash-out refis as interest rates rise.

Finally, the fact that most homeowners underestimate what their home is worth (and thus how much equity they have) is yet another factor that points to the untapped potential for home equity lending. In a recent survey, four out of five homeowners underestimated the amount of value their home has gained over the past three years. And one out of four who do think their home has increased in value said it has increased between one percent and five percent — but the average increase nationally during this time is closer to 10 percent.

CLOSED END HOME EQUITY VS HELOC OUTSTANDING BALANCES (\$ BILLIONS)



Source: SNL Financial

THE FUTURE OF CLOSED-END HOME EQUITY LOANS?

An interesting recent development in home equity lending is the exit from some types of home equity loan products by two of the nation's biggest banks: Bank of America and Wells Fargo. In particular, these banks will no longer offer closed-end (or term) home equity loans. They will continue to offer HELOCs, including a fixed-rate HELOC that enables borrowers to lock in a fixed rate on a portion of the line or the entire approved loan amount.

One of the main reasons for this decision is the fact that closed-end home equity loans are subject to the TILA-RESPA Integrated Disclosures rule (or TRID) that took effect last October. More specifically, under the QM rule, home equity loans must pass the ATR test. However, HELOCs do not have to comply with TRID. Wells Fargo cited this reason specifically in explaining why it would no longer offer closed-end home equity loans, while BofA simply said that it is working on simplifying its home equity product offerings.



The exit of Wells Fargo and BofA from closed-end home equity loans actually reflects a long-term consumer trend in which homeowners are moving away from traditional home equity closed-end in favor of HELOCs. At the big four banks (Wells Fargo, BofA, Citigroup and JPMorgan Chase), closed-end loans account for only 12 percent of their total home equity book. In 2007 this was 30 percent and in 2000 it was 40 percent.

LEGACY LOAN RESETS: STILL A CONCERN?

There has been some concern in the industry about the resets of legacy home equity loans and lines of credit that were made before the crash. More than 12.2 million HELOCs were originated between 2004 and 2007, many using relatively loose underwriting standards and some allowing borrowers to make interest-only payments during the first 10 years.

The concern is that borrowers' monthly HELOC payments will skyrocket when these lines hit the 10-year mark and fully amortizing principle repayment requirements kick in. According to RealtyTrac, the average payment shock from a HELOC reset is around \$150 a month. So far, however, these fears haven't materialized. Through November of last year, the average monthly delinquency rate (30 or more days overdue) was just 2.0 percent, which was the lowest level in eight years.

This has been attributed primarily to the fact that some banks are being proactive in modifying these decade-old HELOCs to help borrowers make their higher payments. For example, banks are offering HELOC refinancing programs that allow borrowers to extend the interest-only period. And many of these HELOCs have been eliminated by first mortgage refinancings that absorbed the outstanding balances. As a result, there are far fewer active legacy HELOCs today than was feared a few years ago.

Another possible problem with these legacy lines is the potentially large number of borrowers whose first mortgages are underwater. Nearly four out of 10

homeowners who were underwater in the third quarter of last year (representing 1.6 million homes) had first and second liens on their homes. These homeowners were underwater by an average of \$83,000.

WHOLE LOAN TRADING IMPLICATIONS

It's worth noting that with the virtual disappearance of the private-label RMBS market in the aftermath of the recession, it has become apparent that new home equity loans will be held on-balance sheet.

While we wait for the non-agency RMBS markets to heal, the primary source of capital for private-label loans will be primarily be whole loan portfolio investors such as banks, and credit unions. In fact, portfolio loans accounted for about a quarter (27 percent) of total 2014 mortgage originations, according to The Housing Finance Policy Center's (HFPC) March 2015 Chartbook. This was the highest level in a decade.

The improving economy is yet another reason why new whole loan portfolio investors will enter the market. Broad-based increases in home prices, falling unemployment and interest rate hikes have lessened concerns about mortgage defaults. These factors have tended to make financial institutions a little less risk-averse and, hence, more willing to view whole loan portfolios as attractive investment opportunities.

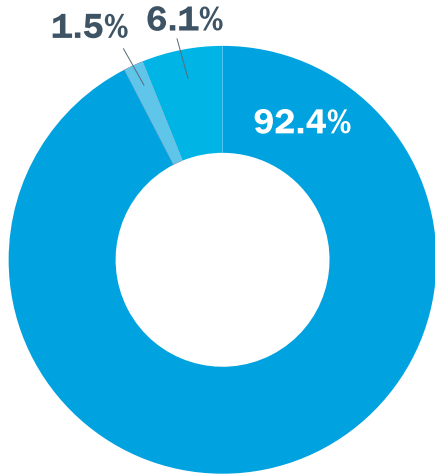
A HEALTHY MARKET ... TODAY AND TOMORROW

Based on these and other trends, it's clear that home equity lending in the U.S. is as healthy today as it has been at any time since before the Great Recession. What's more, these trends paint a generally positive picture for home equity lending in the future.



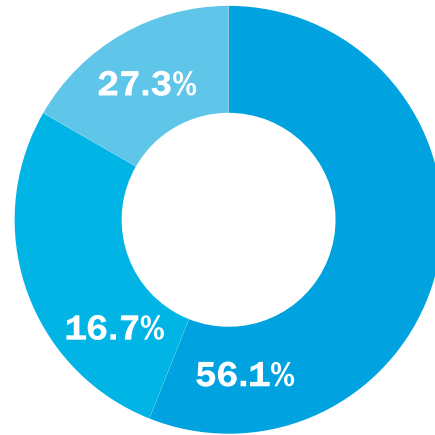
CREDIT STANDARDS AND DEMAND FOR HELOC'S – SENIOR LOAN OFFICER SURVEY

Over the past three months how have your bank's credit standards for approving applications for revolving home equity lines of credit changed?



Tightened considerably	0.0%
Tightened somewhat	1.5%
Remained basically unchanged	92.4%
Eased somewhat	6.1%
Eased considerably	0.0%

Over the past three months how has demand for revolving home equity lines of credit changed?



Substantially weaker	0.0%
Moderately weaker	16.7%
About the same	56.1%
Moderately stronger	27.3%
Substantially stronger	0.0%

Source: Federal Reserve Board: April 2016 Senior Loan Officer Opinion Survey on Bank Lending Practices
All Federally Insured Banks



TOP 20 BANKS WITH THE HIGHEST BALANCE OF HOME EQUITY ASSETS

RANKING	COMPANY NAME	CITY	STATE	HOME EQUITY LOANS & HELOCS
1	Bank of America Corporation	Charlotte	NC	75,753,000
2	Wells Fargo & Company	San Francisco	CA	71,479,000
3	JPMorgan Chase & Co.	New York	NY	56,961,000
4	Citigroup Inc.	New York	NY	24,723,000
5	PNC Financial Services Group, Inc.	Pittsburgh	PA	21,508,881
6	U.S. Bancorp	Minneapolis	MN	16,831,000
7	Citizens Financial Group, Inc.	Providence	RI	16,984,010
8	SunTrust Banks, Inc.	Atlanta	GA	13,011,986
9	TD Group US Holdings LLC	Wilmington	DE	9,561,370
10	BB&T Corporation	Winston-Salem	NC	8,846,126
11	Regions Financial Corporation	Birmingham	AL	8,343,013
12	Fifth Third Bancorp	Cincinnati	OH	7,723,571
13	KeyCorp	Cleveland	OH	7,312,618
14	Huntington Bancshares Incorporated	Columbus	OH	6,585,948
15	M&T Bank Corporation	Buffalo	NY	5,990,256
16	Santander Holdings USA, Inc.	Boston	MA	5,875,052
17	United Services Automobile Association	San Antonio	TX	5,399,179
18	BMO Financial Corp.	Wilmington	DE	4,228,230
19	First Hawaiian, Inc.	San Francisco	CA	3,625,777
20	HSBC North America Holdings Inc.	New York	NY	3,744,849

Source: SNL Financial
Balances represent total home equity (closed end second + HELOCs)



TOP 20 CREDIT UNIONS WITH THE HIGHEST BALANCE OF HOME EQUITY ASSETS

RANKING	COMPANY NAME	CITY	STATE	HOME EQUITY LOANS & HELOCS
1	Navy Federal Credit Union	Vienna	VA	2,207,952
2	Boeing Employees Credit Union	Tukwila	WA	2,084,344
3	Pentagon Federal Credit Union	Alexandria	VA	1,728,269
4	ESL Federal Credit Union	Rochester	NY	1,091,010
5	First Technology Federal Credit Union	Mountain View	CA	1,017,546
6	Bethpage Federal Credit Union	Bethpage	NY	947,580
7	State Employees' Credit Union	Raleigh	NC	718,368
8	SchoolsFirst Federal Credit Union	Santa Ana	CA	685,425
9	Digital Federal Credit Union	Marlborough	MA	672,393
10	Randolph-Brooks Federal Credit Union	Live Oak	TX	540,894
11	Nassau Educators Federal Credit Union	Westbury	NY	533,708
12	Members 1st Federal Credit Union	Mechanicsburg	PA	495,120
13	Alliant Credit Union	Chicago	IL	462,105
14	University of Iowa Community Credit Union	North Liberty	IA	438,171
15	Police and Fire Federal Credit Union	Philadelphia	PA	425,186
16	State Employees Credit Union of Maryland, Inc	Linthicum	MD	417,774
17	Hudson Valley Federal Credit Union	Poughkeepsie	NY	394,213
18	Empower Federal Credit Union	Syracuse	NY	391,137
19	Veridian Credit Union	Waterloo	IA	378,431
20	Allegacy Federal Credit Union	Winston-Salem	NC	377,863

Source: SNL Financial
Balances represent total home equity (closed end second + HELOCs)



TOP 20 BANKS WITH THE HIGHEST PERCENTAGE OF HOME EQUITY TO TOTAL ASSETS

RANKING	COMPANY NAME	CITY	STATE	HOME EQUITY LOANS & HELOCS (\$'000)	TOTAL ASSETS (\$'000)	% OF ASSETS
1	American Investors Bank and Mortgage	Eden Prairie	MN	55,918	93,933	60%
2	Home Loan Investment Bank, F.S.B.	Warwick	RI	55,799	225,999	25%
3	Stonebridge Bank	Minneapolis	MN	50,194	208,988	24%
4	Guaranty Bank (MHC)	Milwaukee	WI	224,186	1,025,077	22%
5	Auto Club Trust, FSB	Dearborn	MI	59,806	319,440	19%
6	Washington Savings Bank	Philadelphia	PA	29,459	159,075	19%
7	NewDominion Bank	Charlotte	NC	55,784	312,446	18%
8	Kennebec Federal Savings and Loan Association of Waterville	Waterville	ME	15,867	89,433	18%
9	Swineford National Bank	Hummels Wharf	PA	52,428	305,202	17%
10	Investment Savings Bank	Altoona	PA	18,814	109,767	17%
11	Providence Bank	Alpharetta	GA	18,608	110,251	17%
12	State Bank of Southwest Missouri	Springfield	MO	17,731	107,631	16%
13	Bank of Holland	Holland	NY	16,113	98,671	16%
14	Bank of Bartlett	Bartlett	TN	56,597	348,320	16%
15	Jersey Shore State Bank	Williamsport	PA	154,005	953,312	16%
16	First Federal Bank, A FSB	Tuscaloosa	AL	18,749	116,376	16%
17	BlueHarbor Bank	Mooreville	NC	25,617	159,589	16%
18	Lee Bank	Lee	MA	50,226	313,828	16%
19	Ohana Pacific Bank	Honolulu	HI	19,053	119,426	16%
20	F&M Bank	Clarksville	TN	137,134	888,326	15%

Source: SNL Financial
Balances represent total home equity (closed end second + HELOCs)




TOP 20 CREDIT UNIONS WITH THE HIGHEST PERCENTAGE OF HOME EQUITY TO TOTAL ASSETS

RANKING	COMPANY NAME	CITY	STATE	HOME EQUITY LOANS & HELOCS (\$000)	TOTAL ASSETS (\$000)	% OF ASSETS
1	Hoboken New Jersey Police Federal Credit Union	Hoboken	NJ	4,476	8,925	50%
2	Blue Cross & Blue Shield of Maine Federal Credit Union	South Portland	ME	3,063	6,318	48%
3	Fairfax County Federal Credit Union	Fairfax	VA	165,269	343,914	48%
4	Members Credit Union	Cos Cob	CT	12,700	27,947	45%
5	Trumbull County Postal Employees Credit Union	Warren	OH	454	1,137	40%
6	Reliance Federal Credit Union	King Of Prussia	PA	9,003	23,142	39%
7	Fairport Federal Credit Union	Fairport	NY	14,563	38,196	38%
8	YS Federal Credit Union	Yellow Springs	OH	6,075	16,245	37%
9	Hamilton Horizons Federal Credit Union	Hamilton	NJ	9,373	25,107	37%
10	Capital Area Taiwanese Federal Credit Union	Rockville	MD	3,822	10,564	36%
11	Health Care Family Credit Union	Richmond Heights	MO	20,461	56,658	36%
12	Direct Federal Credit Union	Needham	MA	173,209	493,532	35%
13	Hingham Federal Credit Union	Hingham	MA	16,197	46,414	35%
14	Blue Water Federal Credit Union	Port Huron	MI	4,777	14,164	34%
15	Meridia Community Federal Credit Union	Hamburg	NY	20,689	62,300	33%
16	LM Federal Credit Union	Baltimore	MD	11,264	34,163	33%
17	Malden Teachers Federal Credit Union	Malden	MA	7,826	23,984	33%
18	Hanscom Federal Credit Union	Hanscom AFB	MA	369,567	1,136,823	33%
19	Palisades Federal Credit Union	Pearl River	NY	50,812	158,748	32%
20	Solon/Chagrin Falls Federal Credit Union	Chagrin Falls	OH	2,558	8,092	32%

Source: SNL Financial
Balances represent total home equity (closed end second + HELOCs)

We're interested in hearing from you. What are your observations about home equity lending, and what do you expect to see in the future?
Send me an email at steven@lendtrade.com.



Steve Schipper, CFA is the Founder and Managing Director of LendTrade, which specializes in helping financial institutions trade whole loans in the secondary market. LendTrade has successfully traded more \$1.5 billion in loans and advised bar  n securitizations of residential and consumer loans. Reach Steve at (515) 778-0199 or steven@lendtrade.com.